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SECURITY INFORMATION

SV/K
IP-344
DATE: 31 August 1953

MEMORANDUM FOR: Deputy Director/Intelligence

THRU : Chief, Economic Research, Research and Reports

THRU : Assistant Director, Research and Reports

SUBJECT : Transmittal of preliminary analysis of the Soviet-East German Protocol of 23 August 1953.

25X1A Attached is a preliminary analysis of the Soviet-East German Protocol of 23 August 1953. The first draft of this memorandum was submitted informally to OCI, GA - IND. [REDACTED] of that office made a number of excellent criticisms and suggestions, which have been incorporated. This version of the analysis has not yet been cleared with OCI.

15/
[REDACTED]
Acting Chief, Analysis Division
Research and Reports

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Security Information

COMMENTS ON THE ECONOMIC ASPECTS OF THE SOVIET-EAST GERMAN PROTOCOL
OF 23 AUGUST 1953

CIA/RR IP-344

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31 August 1953

CENTRAL INTELLIGENCE AGENCY

Office of Research and Reports

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COMMENTS ON THE ECONOMIC ASPECTS OF THE SOVIET-EAST GERMAN PROTOCOL OF
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Introduction

The "Protocol on the termination of collection of German reparations and on other measures to ease the financial-economic obligations of the German Democratic Republic connected with the consequences of the war" 1/ seems to have two purposes, both of which, if successful, would further the Soviet aim of keeping Western Germany out of the European defense community. One purpose is apparently to bolster the East German government, whose prestige was severely shaken by the uprising on 17 June and subsequent disorder. The Protocol is also an attempt to induce the West German electorate to reject Adenauer's party in the coming elections and to increase sentiment in West Germany for accepting the Soviet Union's proposal on German unification.

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The point of course is that the Soviets will ask at the peace conference for equal representation of the present Communist government of East Germany in the all-German government which will supervise the elections, which under such circumstances might well not be free. The Soviet concessions announced in the Protocol represent a considerable departure from the main line of post-war Soviet economic policy with respect to Germany. This policy was characterized by the subordination of all other policy objectives to the objective of a maximum exploitation of the economic resources of East Germany. This policy persisted. The Soviet Union's policy is exemplified by the fact that reparations orders received top priority in the procurement of raw materials until the fall of 1952 when they were demoted to second place by orders for the East German army. 3/ This emphasis on reparations is probably the principal reason for the persistent failure to fulfill the investment part of the East German Five Year Plan. The concessions announced in the Protocol are, however, quite consistent with the "New Course" announced by the SED (Socialistische EinheitsPartei Deutschlands--the Communist Party of East Germany) on

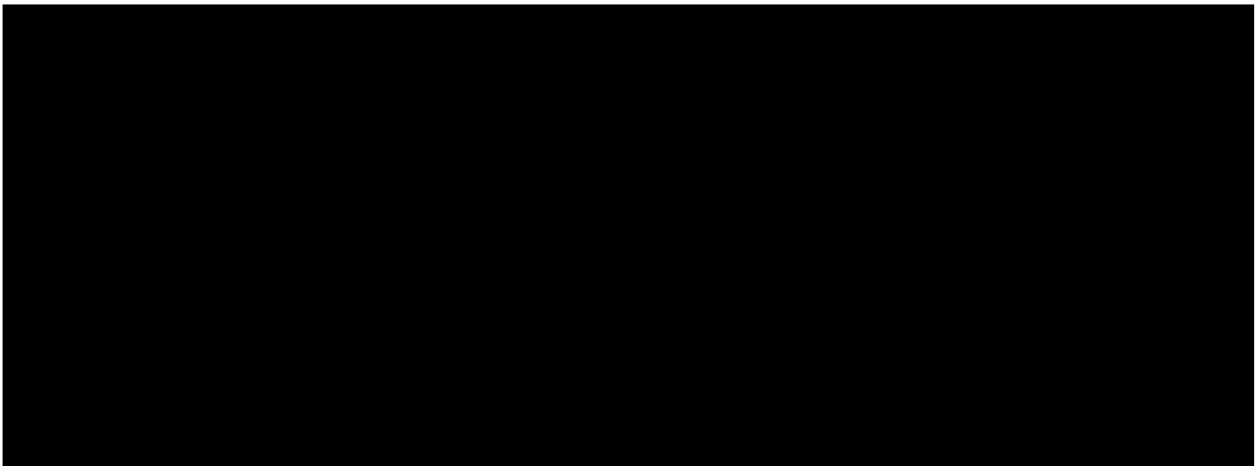
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10 June 1953. In fact, Grotewohl mentions the Protocol as part of the "New Course." 4/ The specific measures announced on 10 June were primarily a reversal of the harsh measures taken in the preceding year to implement the SED's decision to proceed with the building of socialism, but they were accompanied by a promise to de-emphasize heavy industry and devote more resources to the production and distribution of consumer goods. 5/

Although the purpose of the Protocol is propaganda, the concessions contained therein are real. Two basic questions arise: (1) how effective are the concessions contained in the protocol as a propaganda device in East and West Germany? and (2) what is the magnitude of the Soviet concessions to East Germany, and how will they affect the economies of each area. This paper will consider first the effectiveness of the Protocol as propaganda and second the economic effects of the concessions.

Summary and Conclusions

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It is also doubtful that anything the Soviets say will affect how the East Germans feel about them. If, however, living conditions improve significantly as a result of the cessation of reparations and other aspects of the "New Course," the East Germans will probably not resume active resistance to the regime.

The economic concessions, if carried out as promised, could result in an appreciable improvement in the East German scale of living. The reduction in reparations and related payments amounts to about 5 percent of the East German gross national product and should cause a more than 10 percent increase in industrial goods available for domestic consumption, export, or investment. Whether the East German government will carry out the promises of the "New Course" and actually increase the supply of consumers' goods at the expense of the investment program is not yet apparent.

The Soviets are giving up large claims that they probably never expected to collect; in fact some of the claims seem to be the latest expression of Soviet inventive genius. The USSR is, in fact, giving up a current income of less than one billion dollars a year. The economic cost to the Soviet Union of the concessions to East Germany can be evaluated only in terms of what the Soviets expect to receive in return. Most likely this is restoration of the authority of the East German Communist government and complete Sovietization and integration of East Germany into the Soviet bloc. A possible, though less likely, goal is an unified, but neutralized, Germany. In either case, they undoubtedly hope to confound the Western Allies and sow disunity among them.

Effectiveness of Concessions as Propaganda

The release of war prisoners, the return of the Soviet Corporations (SAGs), the cessation of reparations payments, and granting of foreign trade credits will probably evoke from most West Germans an expression to the effect that it's about time. It could be pointed out (1) that the Western Allies had returned virtually all prisoners of war by 1947; (2) that they never contemplated or recognized the legitimacy of Russia taking reparations from current production; 6/ (3) that they never agreed to the \$10 billion claimed by the USSR as reparations; 6/ (4) that conversion of German plants to Soviet ownership was contrary to Allied agreements; 7/ and (5) that in the postwar years US aid to Western Germany amounted to \$3.2 billion, of which only \$1.2 billion is to be repaid, and that British and French claims for aid of more than half a billion were similarly scaled down. 8/

The propaganda motive of the USSR in forgiving debt incurred for external occupation expenditure and other debt incurred in postwar years (except for obligations resulting from trade agreements) is made clear by Grotewohl in a speech in Moscow where, in speaking of the West German debt settlement, he said, "If the proposal of the Soviet Union is accepted, then West Germany would be free from the obligation to pay DM 227 million a year until 1958, and indeed DM 450 million a year as from 1958 regarding amortization and interest." 9/ Just what these external occupation costs are for, it is hard to imagine. In his speech before the Volkskammer on August 25, Grotewohl said that this external debt amounted to DME 25 billion for East Germany alone. He went on to say, "The Western powers have not yet published their figures on this special account, but they are incomparably higher... and Germany, namely the whole of Germany, has been relieved of payment to the Soviet Union of State postwar debts." 10/ These debts might possibly be for the cost of transporting Soviet supplies, or the ruble pay of the Soviet troops in Germany, or even the entire cost of keeping Soviet "supply troops" in the other European satellites. Whatever the nature of these debts, they have not been disclosed heretofore, and it is unlikely that their counterpart could be found in the postwar financial accounts of the Western Allies.

Only in the statement on the reduction of occupation costs do the Soviets have a propaganda weapon that really hits home. Grotewohl states that in 1953 West German occupation costs amounted to DM 9.7 billion, or "34.5 percent of the total budgetary income." 11/ The implied contrast is with the statement in the protocol to the effect that Soviet occupation costs will be reduced to 5 percent of the state budget. The first statement is, at best, only half true and the second does not represent a valid comparison. West German expenditures budgeted for occupation costs and defense in the fiscal year beginning April 1, 1953 amounted to DM 9.9 million. 12/ Compared with the Federal budget only, which amounts to DM 23.5 million for the same period, occupation costs and defense expenditures comprise 42.2 percent. Although the percentages do not check exactly, this must have been the comparison Grotewohl had in mind. The budget of the German Democratic Republic includes, however, the receipts and expenditures of local governments, the state social insurance funds, and most important of all, the nationalized industry. West German occupation costs and defense expenditures amount to 19.3 percent of the combined Federal, Lander (provincial), local and social insurance budgets. 13/

The only way to allow for the inclusion of the nationalized industry in the East German budget is to compare occupation costs, not as a percentage of governmental budgets, but as a percentage of the gross national products (GNP) of the respective areas. Only 1952 figures are available for this purpose. The GNP of East Germany for 1952 is estimated at DME 40.3 billion in 1950 prices. It is assumed that occupation costs were the same in 1952 as 1953, i.e., DME 1,950 million. No adjustment is made for price changes because, while 1952 prices are probably 15 percent higher than 1950, it is also likely that the Soviets account for a part of occupation costs in 1944 prices. As a rough estimate, therefore, Soviet occupation costs in 1952 amounted to 4.8 percent of GNP. The GNP of West Germany in 1952 was DM 128.9 billion. 14/ Occupation costs, minus occupation investment, amounted to DM 5.7 billion. Occupation costs therefore amounted to 4.4 percent of GNP, or about the same as in East Germany. On the basis, occupation cost per occupation soldier, Soviet occupation costs, however, are far lower than Allied occupation costs. 15/

Economic Effects of Concessions on East Germany

It is ironic that the Soviets cannot claim credit for all of the economic benefits accruing to East Germany from the cessation of reparations deliveries and return of the SAG's, because they have never admitted to taking out so much. On May 16, 1950 the Soviet News Agency announced that total Soviet reparation demands had been reduced from \$10,000 million demanded at Yalta to \$6,829 million in 1938 prices, but that only \$3,658 million would have been paid by the end of 1951. Thus \$3,171 million

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remained to be paid by 1965. 16/ The protocol of August 23 announced that \$2,537 million would remain to be paid at the end of 1953, and it was this amount that was cancelled. 17/ The Soviets thus claim that only \$634 million in reparations will have been paid in 1952 and 1953. Converted at DM 2.5 to the dollar (the 1938 rate said to be used by the Soviets) 18/ and increased by 50 percent to allow for price increases, this amounts to DME 2,378 million in current prices or DME 1,189 million each year. Together with admitted occupation costs, the total admitted takings amount to about DME 3,140 million each year. This is about the same as the estimate from budget data for these two items made by HICOG Berlin for 1950 and 1951. 19/ HICOG points out, however, that a complete accounting for the Soviet take from the East German economy must include several other items, e.g., mysterious transfers of DME 400 million in 1950 and DME 600 million in 1951 to the Soviet-owned Guarantee and Credit Bank. These items may be to cover the cost of the uranium mining project, SAG Wismut. Other items that should be included in an estimate of the Soviet take are profits of the SAG's estimated at DME 600-700 million a year, rent paid by the SAG's, transportation costs, and withdrawals from Soviet accounts with the Deutsche Notenbank. 20/ These latter accounts resulted from the one to one conversion of Reichs marks captured or printed by the Soviets immediately after the war. Altogether HICOG, Berlin, conservatively estimates the Soviet take in 1950 and 1951 at DM 4 to 4.5 billion a year.

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The SPD arrives at a figure for reparations (not including occupation costs) of \$28 billion for the period 1945 through 1952. Their use of the conversion rate of 2.5 marks to the dollar for the entire amount is open to question, but even five to the dollar (the current official rate is one DM equals \$0.30) would make the SPD estimate of total reparations \$14 billion paid through 1952, 22/ compared with a Soviet claim of only \$3 billion.

Using the figure of DME 4.5 billion as total Soviet takings a year and deducting DME 2 billion for occupation costs and the cost of running SAG Wismut, which was not returned, East Germany will be relieved of yearly payments of about DME 2.5 billion. This figure of DME 2.5 billion perhaps ought to be reduced by the amount of Soviet investment in the SAG's. How much this investment has been yearly, and to what extent it has been offset by East German subsidies to the SAG's is very much a moot question, so pending receipt of further information on this subject, DME 2.5 billion is taken as a working estimate of the yearly financial gain to East Germany resulting from the concessions contained in the protocol. DM 2.5 billion represents 5 percent of estimated GNP at current prices. 23/ Since almost all reparations are industrial goods, the reduction in reparations and related payments will mean about a 10 percent increase in industrial goods available for domestic consumption, export, or investment. 24/ Whether the East German government will carry out the promises of the "New Course"

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and actually increase supplies of consumers' goods at the expense of the investment program is not yet apparent. The bulk of reparations shipments have consisted of machinery and fine mechanics and optics, a good part of which could probably find a ready market in the Western world. It is doubtful, however, that there will be any appreciable shift of East German trade in this direction. It is more likely that goods formerly shipped as reparations will now be exported to the USSR and the Soviet bloc. The nature of the goods received by the East Germans in return and the use made of them will determine the economic effects of the concessions on the East German economy. The Soviets also promise to supply 75 percent of the food for their occupation troops; whether this concession is included in the reduction of occupation costs is not known.

The credit of about \$60 million a year for two years extended by the Soviet Union to East Germany is not quite as great a boon as it appears, because there is considerable evidence that the Soviet Union receives illegitimate benefits from East Germany through preferential pricing in foreign trade.^{25/} On the basis of trade data contained in ORR contribution to NIE 87 (which are understated if anything) and accounts in the East German press of the percentage increase in trade expected under the 1953 trade agreement with the USSR, it is estimated that the loan will permit East Germany to increase imports from the Soviet Union from about \$250 million a year to \$310 million. ^{26/}

Economic Cost of Concessions to the USSR

The concessions of the Soviet Union will result in a financial sacrifice of \$750 million a year beginning in 1954 for reparations and related payments, including the profits of the SAGs. The value of the SAGs just returned, plus the amount owed on the 66 SAGs returned in May 1952 was stated to be DEM 3,130 million, or \$939 million at the official exchange rate of one DEM equals \$0.30. The credit of \$60 million a year for two years is to be repaid beginning at the end of the second year at 2 percent interest. It is doubtful that the Soviet Union ever intended to collect the DEM 25 billion debt for external occupation costs which they have forgiven the East Germans. This can be viewed as a propaganda maneuver only. In turning back to German control virtually all of the SAGs* the Soviets relinquish a measure of direct control over East German industry. They probably believe that the same results can be achieved through political means.

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* Thirty-five were believed to remain after the return of 66 in May 1952;^{27/} the Soviets have announced the return of 33. This discrepancy may merely result an error in counting the number remaining after May 1952. The full list of those returned under the Protocol has not been published by the East German government.

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Footnotes

RM means Reichsmark

DM means Deutsche Mark East

DM alone or DMW means Deutsche Mark West

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- 8/ The New York Times, February 28, 1953 (U)
- 9/ FBIS, USSR and Eastern Europe, 1953, No. 165, p. EE 11. (R)
- 10/ FBIS, USSR and Eastern Europe, 1953, No. 167, p. EE 19. (R)
- 11/ FBIS, No. 165, op. cit. p. EE 11. (R)
- 12/ Vierteljahrsheft zur Wirtschaftsforschung, 1953, Erstes Heft, "Quantitative Betrachtungen zur Wirtschaftslage in West Deutschland" von Ferdinand Grünig, pl 37. (U)
- 13/ Ibid. p. 39.
- 14/ Exact figures on Allied troops in West Germany were not located, but they would have to number more than one million to equal the Soviet's occupation costs on a per head of soldier basis. RL
- 15/ Vierteljahrsheft zur Wirtschaftsforschung, Zweites Heft 1953, "Die Ergebnisse der vierteljährlichen Volkswirtschaftlichen Gesamtrechnung für die Bundesrepublik." von Ferdinand Grünig und Harry Schimmler 25X1A
pp. 127-133. (U)
- 16/ J. P. Hettl, The Eastern Zone and Soviet Policy in Germany, 1945-50, p. 255. (U)
- 17/ [REDACTED]
- 18/ Vorstand der Sozialdemokratischen Partei Deutschlands, Die Reparationen in der Sowjet-zone von 1945-1952, pp. 31-39. (U)
- 19/ [REDACTED] 25X1A
- 20/ Ibid.
- 21/ Vorstand der Sozial Demokratischen Partei Deutschlands, op. cit. p. 38. (U)
- 22/ Ibid.
- 23/ OSR Project 14.1, Soviet Bloc National Accounts, Part V, Table VIII (V). (S)
- 24/ OSR Project 14.1, op. cit., Part VI, Table V (VI). (S)
- 25/ OSR Contribution to MIB 87, p. 76. (S)
- 26/ [REDACTED]
- 27/ Bundesministerium für gesamtdeutsche Fragen, Die Sowjetische Hand in der Deutschen Wirtschaft, p. 82. (U) 25X1A

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